

## Message Text

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ACTION TRSE-00

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-----211117Z 126188 /12

P 210147Z JAN 77

FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 5112

INFO AMEMBASSY RANGOON PRIORITY

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USADB

FOR NAC AGENCIES

E.O. 11652: ADS, DECLAS 4/21/77

TAGS: EAID, EFIN, BM

SUBJECT: PROPOSED ADB LOAN FOR FORESTRY PROJECT (BURMA)

SUMMARY: ADB MANAGEMENT PROPOSES \$25.1 MILLION EQUIVALENT  
LOAN FROM SPECIAL FUNDS TO GOVERNMENT OF BURMA TO FINANCE  
FOREX COST OF A FORESTRY PROJECT AIMED AT THE REHABILITATION  
AND IMPROVEMENT OF TIMBER EXTRACTION OPERATIONS IN UPPER  
CENTRAL BURMA. PRINCIPAL OBJECTIVES ARE TO INCREASE  
FOREIGN EXCHANGE EARNINGS FROM TEAK EXPORTS AND SUPPLY  
DOMESTIC MARKET WITH NON-TEAK SAWNWOOD. PROJECT CONCENTRATES  
ON ROAD CONSTRUCTION AND UPGRADING, REHABILITATION OF  
LOGGING AND TRANSPORT EQUIPMENT, AND SAWMILL MODERNIZATION.  
USADB RECOMMENDS FAVORABLE NAC ACTION.

1. ADB DOC. R33-77 WITH ATTACHMENTS DESCRIBING PROPOSED  
LOAN POUCHES ADDRESSEES JANUARY 17. BOARD CONSIDERATION  
SCHEDULED FEBRUARY 8, 1977.  
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2. ADB MANAGEMENT PROPOSING \$25.1 MILLION LOAN FROM  
SPECIAL FUNDS TO GOVERNMENT OF BURMA. PROCEEDS WILL  
FINANCE FOREX COST OF (A) CONSTRUCTION AND UPGRADING OF  
ACCESS AND FEEDER ROADS; (B) REHABILITATION OF LOGGING  
AND TRANSPORT EQUIPMENT, PROVISION OF NEW EQUIPMENT FOR  
LOG EXTRACTION, PROVISION OF SPARE PARTS, AND CONSTRUCTION

OF TUGBOATS; (C) REHABILITATION AND/OR CONSTRUCTION OF SAWMILLS; (D) PROVISION OF VEHICLES AND DIESEL ENGINES; (E) STAFF TRAINING; AND (F) CONSULTANT SERVICES. PROPOSED TERMS ARE 40 YEARS AMORTIZATION INCLUDING 10 YEAR GRACE PERIOD, 1 PERCENT SERVICE CHARGE. GOVERNMENT OF BURMA TO BE BORROWER, TIMBER CORPORATION (TC), A STATE CORPORATION ADMINISTRATIVELY UNDER THE MINISTRY OF AGRICULTURE AND FORESTS, TO BE EXECUTING AGENCY.

3. FORESTS COVER 57 PERCENT OF BURMA'S LAND AREA PROVIDING AN AREA OF OPERABLE CLOSED FOREST EXCEEDED ONLY BY INDIA AND INDONESIA, AMONG BANK'S DEVELOPING MEMBER COUNTRIES (DMC'S). SINCE BURMA'S FORESTS CONTAIN 75 PERCENT OF WORLD'S STANDS OF NATURAL TEAK, THEY HAVE POTENTIAL WORTH WELL BEYOND THAT OF ANY COUNTRY IN ASIA-PACIFIC REGION. DESPITE THIS POTENTIAL, INDUSTRIAL ROUNDWOOD PRODUCTION IN ONLY ABOUT 2 PERCENT OF TOTAL HARVEST IN BANK'S DMC'S V SAWNWOOD PRODUCTION LESS THAN 4 PERCENT OF REGION TOTAL; AND EXPORTS IN VOLUME TERMS WELL BEHIND OTHER FOREST-RICH REGION COUNTRIES. FORESTRY INDUSTRY IN BURMA HAS GROWN AT RATE OF ABOUT ONE PERCENT P.A., CURRENTLY ACCOUNTS FOR ABOUT 2.5 PERCENT OF GDP.

4. PRODUCTION TRENDS AND MARKETING CONSIDERATIONS DIFFER IN SIGNIFICANT RESPECTS AS BETWEEN TEAK AND NON-TEAK HARDWOODS:

A. TEAK - PRODUCTION FELL FROM PRE-WAR LEVEL OF 800,000 TO 230,000 CU.M. IN 1950-51, ROSE TO 720,000 CU.M. IN 1970/71, THEN DECLINED TO 562,000 CU.M. LIMITED OFFICIAL USE

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IN 1975/76. PRESENT PRODUCTION LEVEL COMPARES WITH ANNUAL ALLOWABLE CUT (AAC; THE VOLUME OF WOOD THAT CAN BE HARVESTED ANNUALLY FROM A PARTICULAR AREA IN PERPETUITY) OF 623,000 CU.M. AND BACKLOG OF GIRDLED TREES (THOSE PREPARED FOR CUTTING UNDER AAC) OF ABOUT 400,000. TEAK SAWNWOOD PRODUCTION WAS 106,000 CU.M. IN 1975/76, HAVING DECLINED IN PROPORTION TO OVERALL TEAK PRODUCTION IN PAST FIVE YEARS. EXPORTS HAVE BEEN FAIRLY CONSTANT AT ABOUT 90,000 CU.M. ACCOUNTING FOR NEARLY ALL OF COUNTRY'S FORESTRY EXPORT EARNINGS OF ABOUT \$38 MILLION (1975/76). WITH WORLD TEAK DEMAND AND PRICES STRONG, BURMA'S ABILITY TO SUPPLY HAS BEEN MAIN CONSTRAINT ON MARKET GROWTH.

B. OTHER HARDWOODS - PRODUCTION PEAKED AT 1,823,000 CU.M. IN 1962/63, DECLINED ERRATICALLY TO 632,000 CU.M. IN 1975/76. LATTER FIGURE COMPARES WITH AAC OF 3,500,000 CU.M. SAWN HARDWOOD PRODUCTION FELL FROM 467,000 CU. M. IN 1972/73 TO 323,000 CU. M. IN 1975/76. EXPORTS WERE ONLY 30,000 CU.M. IN 1974/75. NON-TEAK

HARDWOODS ARE INTENDED PRIMARILY FOR DOMESTIC MARKET,  
BUT PRODUCTION IS CURRENTLY WELL SHORT OF DEMAND

5. FORESTRY INDUSTRY'S PRINCIPAL PROBLEM IS DECLINING  
CAPACITY AT EACH STATE OF PRODUCTION. PAST RELIANCE ON  
ANIMALS FOR HAULING HAS ENCOUNTERED INCREASING DIFFI-  
CULTIES IN ACQUIRING BUFFALOES OWING TO COMPETING DEMANDS  
FROM AGRICULTURE; EXISTING MOTORIZED EQUIPMENT IS IN  
GENERAL STATE OF DISREPAIR; ROADS ARE INADEQUATE; AND  
MOST SAWMILLS ARE OBSOLETE AND INEFFICIENT. IN ADDITION,  
MANAGEMENT OF THE TIMBER CORPORATION HAS BEEN DEFICIENT  
IN SEVERAL RESPECTS. AS RESULT OF THESE FACTORS, LOSS  
AND WASTAGE FROM POINT OF FELLING TO FINAL PRODUCTION  
HAS BEEN EXTREMELY HIGH: ABOUT 15 PERCENT OF TREES  
LEFT IN THE FOREST; ANOTHER 30 PERCENT LOST EN ROUTE TO

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FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 5113

INFO AMEMBASSY RANGOON PRIORITY

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LEFT IN THE FOREST; ANOTHER 30 PERCENT LOST EN ROUTE TO  
SAWMILLS; A SUBSTANTIAL DEGRADE IN THE MILLING  
PROCESS; AND UNKNOWN FURTHER LOSSES IN MOVING LUMBER TO  
MARKET.

6. WELL AWARE OF PROBLEMS, GOVT HAS ACCORDED HIGH  
PRIORITY TO FORESTRY IN BURMA'S FIVE-YEAR DEVELOPMENT  
PROGRAM (1977/78 - 81/82. PLAN CALLS FOR EXPENDITURE  
OF \$126.2 MILLION EQUIVALENT FOR MODERNIZATION  
FORESTRY SECTOR, REPRESENTING ABOUT 4.5  
PERCENT OF TOTAL PLAN INVESTMENT. MANAGEMENT REFORMS  
ARE BEING TAKEN IN CONTEXT OF ONGOING COMMERCIALIZATION  
POLICY FOR STATE ENTERPRISES.

7. BANK MISSION IN 1973 CONCLUDED THAT THERE WAS CONSIDERABLE SCOPE FOR FORESTRY DEVELOPMENT IN BURMA, BUT THAT DETAILED PREPARATORY WORK REQUIRED TO DEVELOP VIABLE PROJECT. SUBSEQUENTLY GOVT DECIDED AWAIT OUTCOME OF SEPARATE NEGOTIATIONS WITH WORLD BANK BEFORE PROCEEDING WITH BANK TA. NEGOTIATIONS RESUMED FOLLOWING APPROVAL OF \$24 MILLION IDA-FINANCED PROJECT IN SOUTH CENTRAL BURMA IN JULY 1974. BANK TA APPROVED IN AMOUNT LIMITED OFFICIAL USE

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OF \$98,000 IN MARCH 1975, AND UK CONSULTANTS DELIVERED FEASIBILITY REPORT IN MAY 1976. BANK MISSION VISITING PROJECT AREA IN JULY 1976 CONCLUDED CONSULTANTS' PROPOSAL NEEDED REVISION IN CERTAIN ASPECTS OF DETAIL. PROPOSED PROJECT IS OUTCOME OF THAT REVISION, BASED ON FIELD INVESTIGATION AND VISITS WITH GOVT OFFICIALS.

8. PROJECT AREA IS LOCATED IN CENTRAL UPPER BURMA, LYING LARGELY BETWEEN THE CHINDWIN AND IRRAWADY RIVERS. IT COMPRISES ALL OF THE SAGAING DIVISION, ONE OF THE LARGEST IN TERMS OF FOREST RESOURCES OF THE TC'S 14 DIVISIONS, EXTENDING NORTH OF MANDALAY FOR SOME 400 KM., RANGING BETWEEN 160 AND 240 KM. IN AN EAST-WEST DIRECTION. IN 1976/76 TEAK PRODUCTION WAS 28 PERCENT AND NON-TEAK HARDWOOD PRODUCTION 37 PERCENT OF COUNTRYWIDE PRODUCTION TOTALS. LAND USE PATTERN OF PROJECT AREA IS ONE OF AGRICULTURE IN ALLUVIAL PLAINS AND RIVER VALLEYS, FORESTRY IN THE HILLS. POPULATION IS ESTIMATED AT 3.1 MILLION OR ONLY 33 PERSONS/SQ. MI. APART FROM MAJOR RIVERS THERE ARE TWO LARGELY NORTH-SOUTH RAIL LINES, BUT NO RAIL OR ALL-WEATHER ROAD LINKAGES FROM EAST TO WEST. TIMBER EXTRACTION, TRANSPORTATION, AND PROCESSING FACILITIES SUFFER FROM SAME GENERAL INADEQUACIES AS DESCRIBED FOR INDUSTRY AS A WHOLE (PARA. 5).

9. PROJECT AIMS AT INCREASING BURMA'S FOREX EARNINGS BY OPTIMUM UTILIZATION OF TEAK RESOURCES IN AREA, AND ENHANCING PRODUCTION OF HARDWOODS PRIMARILY TO SATISFY DOMESTIC DEMAND, THROUGH IMPROVEMENT OF EXTRACTION, TRANSPORT AND MARKETING OF SAGAING DIVISION AND REHABILITATION AND MODERNIZATION OF PROCESSING FACILITIES IN PROJECT AREA. PRODUCTION TARGETS ARE FOR INCREASES AS FOLLOWS:

(A) TEAK, FROM PRESENT (I.E. 1976/77, AS ESTIMATED) LEVEL OF 112,000 CU. M. TO ANNUAL AVERAGE OF LIMITED OFFICIAL USE

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140,000 CU. M.;

(B) HARDWOOD, FROM PRESENT LEVEL OF 240,000 CU. M.  
TO 336, 000 CU. M.;

(C) SAWN TIMBER, FROM PRESENT LEVEL OF 75,000 CU. M.  
TO 113,000 CU. M. BY 1981/82.

10 PROJECT CONSISTS OF FOLLOWING COMPONENTS:

(A) ROADS - CONSTRUCTION OF 160 KM. OF ACCESS AND  
2,100 KM. OF FEEDER ROADS; AND UPGRADING OF 100  
KM. OF FAIR-WEATHER TO ALL-WEATHER ROADS.

(B) FOREST OPERATIONS - REHABILITATION OF EXISTING  
LOGGING AND HAULAGE EQUIPMENT; PROCUREMENT OF NEW  
EXTRACTION EQUIPMENT AND HAULAGE TRUCKS; PROVISION OF  
SPARE PARTS FOR EXISING TUGBOATS/LAUNCHES AND CONSTRUCTION  
OF 20 NEW TUGBOATS; AND ESTABLISHMENT OF FIVE WORKSHOPS.

(C) SAWMILLING - REHABILITATION AND MODERNIZATION  
OF EXISTING SAWMILLS; PROVISION OF 10 MOBILE SAWMILLS;  
ESTABLISHMENT OF WORKSHOPS.

(D) FOREST DEPARTMENT - PROCUREMENT OF INSPECTION  
VEHICLES AND MARINE DIESEL ENGINES, AND PLANTING OF TEAK  
SEEDLINGS.

(E) TRAINING AND FELLOWSHIPS.

(F) CONSULTING SERVICES - FOUR EXPERTS IN THE AREAS  
OF MAINTENANCE ENGINEERING (3 YEARS), ROAD CONSTRUCTION  
(3 YEARS), HARDWOOD UTILIZATION AND SAWMILLING (1 1/2 YEARS),  
AND MANAGEMENT ACCOUNTING (2 1/2 YEARS).

(G) PROJECT ADMINISTRATION - ESTABLISHMENT OF PROJECT  
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HEADQUARTERS AT MANDALAY WITH NECESSARY  
FACILITIES AND RECRUITMENT OF ADDITIONAL QUALIFIED PROJECT STAFF.

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FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 5114

INFO AMEMBASSY RANGOON PRIORITY

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11. PROCUREMENT OF GOODS AND SERVICES WILL BE IN ACCORDANCE WITH BANK'S GUIDELINES. SUPPLY CONTRACTS FOR TRACTORS, EXTRACTION EQUIPMENT, TRUCKS, SAWMILL EQUIPMENT, WORKSHOP EQUIPMENT AND CONSTRUCTION EQUIPMENT (INCLUDING SPARES FOR NEW EQUIPMENT AND EXISTING SAWMILLS) WILL BE AWARDED ON BASIS OF INTERNATIONAL COMPETITIVE BIDDING. SMALLER CONTRACTS WILL BE AWARDED ON BASIS OF BIDS ON QUOTATIONS FROM REASONABLE NUMBER OF SUPPLIERS FROM MORE THAN ONE COUNTRY. HOWEVER, SINCE INTERNATIONAL BIDDING IS INAPPROPRIATE FOR PURCHASE OF SPARES FOR EXISTING MACHINES AND EQUIPMENT, IT IS RECOMMENDED THAT SUCH ITEMS BE PURCHASED DIRECT FROM MANUFACTURERS OF THE ORIGINAL EQUIPMENT OR THEIR AGENTS. AN AMOUNT OF \$1,576,000 HAS BEEN SET ASIDE FOR THIS PURPOSE.

12. TOTAL PROJECT COST IS ESTIMATED AT \$44.2 MILLION, OF WHICH \$25.1 MILLION FOREX AND \$19.1 MILLION LOCAL CURRENCY. BANK PROPOSES FINANCE ALL OF FOREX PORTION. PROCEEDS, EXCEPTING \$170,000 RELATING TO THE FORESTRY DIVISION (FD), WILL BE RELENT BY GOVT TO TC AT 9 PERCENT INTEREST, WITH REPAYMENT PERIOD OF 15 YEARS INCLUDING 5 YEAR GRACE PERIOD. THE \$170,000 TO THE FD (FOR  
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INSPECTION VEHICLES AND DIESEL ENGINES TO BE USED FOR CONSTRUCTION OF INSPECTION BOATS) WILL BE CHanneled THROUGH THE NORMAL GOVT BUDGET SYSTEM. GOVT AND TC WILL PROVIDE LOCAL CURRENCY REQUIREMENTS AS NEEDED. ABOUT 65 PERCENT OF LATTER ARE FOR TRANSPER PAYMENTS SUCH AS IMPORT DUTIES AND TAXES. GOVT AND TC HAVE ASSURED THAT

FUNDS WILL BE MADE AVAILABLE FOR SPARE PARTS AND EQUIPMENT  
REPLACEMENT AFTER PROJECT COMPLETION.

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FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 5115

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13. TC, EXECUTING AGENCY FOR PROJECT, IS REGARDED AS  
HAVING A COMMENDABLE RECORD WITH REGARD TO TEAK PRODUCTION  
OVER PAST DECADE, BUT ACHIEVEMENTS HAVE BEEN LESS NOTE-  
WORTHY IN HARDWOOD; ACHIEVEMENTS OF MILLING AND MARKETING  
DEPARTMENT HAVE LEFT MUCH TO BE DESIRED; AND MANAGEMENT  
PERFORMANCE ON THE WHOLE HAS BEEN UNSATISFACTORY. MAJOR  
SHORTENINGS HAVE BEEN: FAILURE TO INTRODUCE EFFECTIVE  
INCENTIVE SCHEME; INADEQUATE PERFORMANCE MONITORING; POOR  
INTER-DEPARTMENTAL COORDINATION; FAILURE TO COMMUNICATE  
POLICES TO LABOR; AND INADEQUATE FINANCIAL MONITORING.

14. SOME OF THESE FAILURES ARE BEING MET AS RESULT OF  
GOVT'S COMMERCIALIZATION POLICY WHICH, WITH EFFECT  
FROM 1975/76 FISCAL YEAR, AIMS TO PUTS OPERATIONS OF STATE  
ECONOMIC ENTERPRISES ON COMMERCIAL BASIS. THESE  
REFORMS HAVE BEEN LARGELY INCORPORATED IN PROJECT PRO-  
VISIONS SUMMARIZED PARA. 17 BELOW.

15. TC WILL BE RESPONSIBLE FOR OVERALL IMPLEMENTATION OF  
PROJECT EXCLUDING THE SMALL FD COMPONENT. TC HAS SUFFICIENT  
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EXPERIENCE IN ALL PHASES OF PROJECT EXCEPT CONSTRUCTION OF ACCESS ROADS, WHICH HAS BEEN HANDLED BY CONSTRUCTION CORPORATION (CC). PROJECT ROADS WILL BE EXECUTED ON FORCE ACCOUNT BASIS BY TC WITH ASSISTANCE OF CC. WITHIN TCN SAGAING DIVISION WILL HAVE RESPONSIBILITY FOR DAY-TO-DAY IMPLEMENTATION OF PROJECT.

16. IDA FORESTRY PROJECT IN LOWER BURMA INCLUDES PROVISION FOR DETAILED EXAMINATION OF ORGANIZATION STRUCTURE AND OPERATION AND MANAGEMENT OF TC. BANK IS TO BE FULLY INFORMED OF PROGRESS OF THESE STUDIES AND GOVT AND TC WILL CONSULT ON IMPLEMENTATION OF MAJOR RECOMMENDATIONS. IN VIEW OF IDA STUDY, RECOMMENDATIONS ON INSTITUTIONAL ASPECTS OF BANK PROJECT ARE LIMITED TO REQUIREMENTS FOR INSURING EFFICIENT IMPLEMENTATION.

17. PROVISIONS FOR STRENGTHENING SAGAING DIVISION INCLUDE: APPOINTMENT OF A PROJECT GENERAL MANAGER, IN CONSULTATION WITH BANK, REPORTING TO MANAGEMENT COMMITTEE OF TC AND RESPONSIBLE FOR OVERALL PROJECT IMPLEMENTATION; REORGANIZATION OF OPERATIONAL AND FINANCIAL MANAGEMENT SYSTEMS AND PROCEDURES, INCLUDING IMPLEMENTATION OF COST CONTROL SYSTEM; STAFF TRAINING AND RECRUITING; INTRODUCTION OF INCENTIVE SCHEMES FOR BOTH INDIVIDUALS AND GROUPS OF PEOPLE, TO SERVE AS BASIS FOR PROMOTION AND PAYMENT OF BONUSES. MANAGEMENT ACCOUNTING CONSULTANT WILL ASSIST IN FORMULATING AND IMPLEMENTING INCENTIVE SCHEMES AND BANK TO BE INFORMED OF THEIR PROGRESS ON QUARTERLY BASIS.

18. TO DIRECT AND ASSIST IN PROJECT IMPLEMENTATION, TWO PROJECT COMMITTEES WILL BE ESTABLISHED: (A) A PROJECT STEERING COMMITTEE (PSC) AT NATIONAL LEVEL, WITH DEPUTY MINISTER OF MINISTRY OF AGRICULTURE AND FORESTRY (MAF) AS CHAIRMAN, TO COORDINATE VARIOUS GOVT AGENCIES ON POLICY MATTERS RELATED TO PROJECT; (B) A PROJECT IMPLEMENTATION COMMITTEE (PIC), WITH PROJECT GENERAL MANAGER AS CHAIRMAN, TO COORDINATE IMPLEMENTATION OF PROJECT. LIMITED OFFICIAL USE

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PROPOSED INSTITUTIONAL ARRANGEMENTS ARE BASICALLY SIMILAR TO THOSE MADE FOR IDA PROJECT, WITH CERTAIN ADDITIONS INCLUDING INCENTIVE SCHEME FOR SAGAING DIVISION.

19. BASED ON WHAT IT BELIEVES TO BE CONSERVATIVE ESTIMATES OF FUTURE PRICE TRENDS, BANK PROJECTS GROSS INCREMENTAL EXPORT EARNINGS ATTRIBUTABLE TO PROJECT AT \$247 MILLION (MOSTLY TEAK) IN 1976 DOLLARS, OR \$200 MILLION ON NET BASIS, OVER THE 10-YEAR LIFE OF THE PROJECT. LATTER FIGURE



APPROXIMATES COUNTRY'S CURRENT ANNUAL EXPORT EARNINGS.  
OTHER PROJECT BENEFITS INCLUDE MEETING PRESENTLY UNSATIS-  
FIED DOMESTIC HARDWOOD DEMAND; PROVISION OF AN ADDITIONAL  
1,600 FULL-TIME AND 1,000 PART TIME JOBS; AND IMPORTANT  
INSTITUTIONAL BENEFITS IN THE PROVISION OF TECHNICAL  
TRAINING AND INTRODUCTION OF MODERN MANAGEMENT TECHNIQUES.

20. PROPOSED PROJECT, WHICH IS IN LINE WITHIN GOVT'S  
POLICY FOR MODERNIZATION AND MECHANIZATION OF FORESTRY  
INDUSTRY, IS BELIEVED TO BE TECHNICALLY SOUND AND ECONOM-  
ICALLY AND FINANCIALLY VIABLE. PROJECT HAS ESTIMATED  
ECONOMIC RATE OF RETURN OF OVER 100 PERCENT, THE EXCEP-  
TIONALLY HIGH RATE REFLECTING THE UNIQUE VALUE OF TEAK AS  
A RESOURCE AND FACT THAT PROJECT, AT LIMITED COSTS, WILL  
REMOVE BOTTLENECKS WHICH CURRENTLY RESTRICT ITS RATIONAL  
UTILIZATION. FINANCIAL RATE OF RETURN TO TC IS ESTIMATED  
AT -14.2 PERCENT, THE RELATIVELY LOW RATE REFLECTING GOVT'S  
POLICY ON PRICING OF TIMBER PRODUCTS, HEAVY TAXATION, AND  
THE EXISTING EXPORT PRICE EQUALIZATION FUND SYSTEM.  
USADB SUPPORTS PROPOSAL AND RECOMMENDS FAVORABLE NAC ACTION.

21. REQUEST RANGOON COMMENTS FOR NAC AGENCIES, INFO USAD  
MANILA, PURSUANT TO STATE 119795 DATED 3 JULY 1972.  
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